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City and County of San Francisco

Office of the Auditor

# AIRPORT COMMISSION:

## Concession Audit of Bay Area Restaurant Group Joint Venture

GOVERNMENT  
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# City and County of San Francisco

Office of the Controller – City Services Auditor

## **AIRPORT COMMISSION:**

### **Concession Audit of Bay Area Restaurant Group Joint Venture**

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*February 19, 2009*

**CONTROLLER'S OFFICE  
CITY SERVICES AUDITOR**

The City Services Auditor was created within the Controller's Office through an amendment to the City Charter that was approved by voters in November 2003. Under Appendix F to the City Charter, the City Services Auditor has broad authority for:

- Reporting on the level and effectiveness of San Francisco's public services and benchmarking the city to other public agencies and jurisdictions.
- Conducting financial and performance audits of city departments, contractors, and functions to assess efficiency and effectiveness of processes and services.
- Operating a whistleblower hotline and website and investigating reports of waste, fraud, and abuse of city resources.
- Ensuring the financial integrity and improving the overall performance and efficiency of city government.

The audits unit conducts financial audits, attestation engagements, and performance audits. Financial audits address the financial integrity of both city departments and contractors and provide reasonable assurance about whether financial statements are presented fairly in all material aspects in conformity with generally accepted accounting principles. Attestation engagements examine, review, or perform procedures on a broad range of subjects such as internal controls; compliance with requirements of specified laws, regulations, rules, contracts, or grants; and the reliability of performance measures. Performance audits focus primarily on assessment of city services and processes, providing recommendations to improve department operations.

We conduct our audits in accordance with the Government Auditing Standards published by the U.S. Government Accountability Office (GAO). These standards require:

- Independence of audit staff and the audit organization.
- Objectivity of the auditors performing the work.
- Competent staff, including continuing professional education.
- Quality control procedures to provide reasonable assurance of compliance with the auditing standards.

Audit Team: Elisa Sullivan, Audit Manager  
Edwin De Jesus, Associate Auditor





**CITY AND COUNTY OF SAN FRANCISCO**  
**OFFICE OF THE CONTROLLER**

**Ben Rosenfield**  
**Controller**  
Monique Zmuda  
Deputy Controller

February 19, 2009

San Francisco Airport Commission  
P.O. Box 8097  
San Francisco International Airport  
San Francisco, CA 94128-8097

President and Members:

The Controller's Office, City Services Auditor, presents its report concerning the concession audit of Bay Area Restaurant Group Joint Venture (Bay Area Group). Bay Area Group has three 10-year lease agreements with the Airport Commission of the City and County of San Francisco. Under the terms of its leases, Bay Area Group operates two restaurants and two quick-serve shops under different business names at the San Francisco International Airport.

**Reporting Period:** February 15, 2005, through December 31, 2007

<b>Fees Paid:</b>	Noah's Bagels and Max's Eatz	\$1,324,807
	Buena Vista Café	1,584,253
	Gordon Biersch	<u>687,626</u>
	<b>Total:</b>	<b>\$3,596,686</b>

**Results:**

Bay Area Group correctly reported gross revenues of \$14,208,072 for its Noah's Bagels and Max's Eatz operations, \$14,002,108 for Buena Vista Café, and \$6,530,213 for Gordon Biersch, for a total of \$34,740,393. Further, Bay Area Group timely paid \$3,596,686 in rent to the Airport Department (Airport). However, the Airport underbilled the Minimum Annual Guarantee (MAG) for Noah's Bagels and Max's Eatz for 22 months, which caused Bay Area Group to pay late its total monthly MAG. Also, for one of its facilities, Bay Area Group did not comply with a lease provision that it maintain its security deposit at one-half of the current MAG; it should have increased its deposit by \$13,103 for 2007. Finally, the Airport should review and clear its accounts receivable records with Bay Area Group. Airport records indicate that Bay Area Group has numerous outstanding invoices and credits totaling a net payment due of \$524, in addition to a large credit of \$79,012 for our audit period. Bay Area Group's controller was not aware of any payments owed or of the large credit.

The responses from the Airport and Bay Area Group are attached to this report. The Controller's Office, City Services Auditor, will follow up with the Airport on the status of the recommendations made in this report.

Respectfully submitted,

Robert Tarsia  
Deputy Audit Director

cc: Mayor  
Board of Supervisors  
Budget Analyst  
Civil Grand Jury  
Public Library

# INTRODUCTION

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## **Audit Authority**

The Office of the Controller (Controller) has authority under the San Francisco Administrative Code, Chapter 10, Article 1, Section 10.6-2 to audit, at regular intervals, all leases of city-owned real property where rent of \$100,000 or more a year is to be paid to the City. In addition, the City Charter provides the Controller, City Services Auditor (CSA), with broad authority to conduct audits. We conducted this audit under that authority and pursuant to an audit plan agreed to by the Controller and the Airport.

## **Background**

Bay Area Restaurant Group Joint Venture (Bay Area Group) operates two restaurants and two quick serve shops under three separate 10-year lease agreements with the Airport Commission (Commission) of the City and County of San Francisco. Under lease number 03-0184, with rent commencement dates of December 7, 2004, and March 15, 2005, Bay Area Group operates the Noah's Bagels (now Max's the Greek) and Max's Eatz quick serve shops at the domestic terminals of the San Francisco International Airport (SFO). Under lease number 03-0202 with a rent commencement date of April 11, 2005, Bay Area Group operates the Buena Vista Café, also at a domestic terminal of SFO. Under lease number 03-0204 with a rent commencement date of December 7, 2004, Bay Area Group operates the Gordon Biersch restaurant in one of the domestic terminals of SFO. The December 2004 commencement date for Max's Eatz and Gordon Biersch, however, changed to February 15, 2005, because both facilities opened at this later date.

The lease agreements require Bay Area Group to pay the Airport Department (Airport) the greater of a Minimum Annual Guarantee (MAG), or a tiered percentage rent of 6 to 12 percent of its annual gross revenues. The Airport can adjust the MAG annually.

## **Scope**

The purpose of this audit was to determine whether Bay Area Group complied with the reporting and payment provisions of its lease agreements with the Commission. Our audit covered the period from February 15, 2005, when the first of Bay Area Group's four facilities opened, through December 31, 2007.

## **Methodology**

To conduct the audit, we examined the applicable terms of Bay Area Group's leases and the adequacy of its procedures for collecting, recording, summarizing, and reporting its gross revenues to the Airport. To determine whether Bay Area Group accurately reported its gross revenues to the Airport, we tested on a sample basis Bay Area Group's monthly sales records, daily sales reports, and bank deposit records. In addition, we determined whether Bay Area Group had any outstanding payments for the period. We also compared the gross revenues reported to the Airport with the gross revenues reported to the California State Board of Equalization for selected calendar quarters, and verified Bay Area Group's compliance with certain other provisions of its lease.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.



# AUDIT RESULTS

## Bay Area Group Correctly Reported Its Gross Revenues and Timely Paid Its Rent Due to the Airport

From February 15, 2005, through December 31, 2007, Bay Area Group correctly reported gross revenues of \$34,740,393 and timely paid \$3,596,686 in rents to the Airport. However, Bay Area Group did not pay the correct monthly Minimum Annual Guarantee (MAG) rent for almost two years for one of its restaurants, due to an Airport billing error. Also, for one of its facilities, Bay Area Group is not in compliance with a lease provision that it maintain its security deposit at one-half of the current MAG. Finally, the Airport has several outstanding accounts receivable transactions that it should update and resolve with Bay Area Group. The exhibit below summarizes Bay Area Group's reported gross revenues and rent paid for its lease agreements.

### EXHIBIT

### Gross Revenues Reported and Rent Paid February 15, 2005, Through December 31, 2007

	February 15, 2005, through December 31, 2005	January 1, 2006, through December 31, 2006	January 1, 2007, through December 31, 2007	Totals
<b>Gross Revenues Reported</b>				
Noah's Bagels & Max's Eatz	\$ 4,070,661	\$ 4,765,173	\$ 5,372,238	\$14,208,072
Buena Vista Café	3,311,928	4,962,979	5,727,201	14,002,108
Gordon Biersch	<u>1,820,776</u>	<u>2,214,410</u>	<u>2,495,027</u>	<u>6,530,213</u>
<b>Total Gross Revenues</b>	<b>\$ 9,203,365</b>	<b>\$11,942,562</b>	<b>\$13,594,466</b>	<b>\$34,740,393</b>
<b>Rent Paid</b>				
Noah's Bagels & Max's Eatz	\$ 375,066	\$ 444,517	\$ 505,224	\$ 1,324,807
Buena Vista Café	365,431	563,558	655,264	1,584,253
Gordon Biersch	<u>186,494</u>	<u>233,729</u>	<u>267,403</u>	<u>687,626</u>
<b>Total Rent Paid</b>	<b>\$ 926,991</b>	<b>\$ 1,241,804</b>	<b>\$ 1,427,891</b>	<b>\$ 3,596,686</b>

Source: Bay Area Group's Annual Statements of Sales and Rent Due

**The Airport Did Not  
Collect the Correct MAG  
for Noah's Bagels and  
Max's Eatz**

We found that the Airport only invoiced and collected from Noah's Bagels and Max's Eatz a monthly Minimum Annual Guarantee (MAG) of \$4,800 from March 2005 through December 31, 2006. This amount, however, was \$2,230 less than the \$7,030 monthly MAG provided for under the lease agreement for the two facilities.

The lease agreement requires Bay Area Group to pay the monthly MAG at the beginning of each month. Bay Area Group then calculates the percentage rent on the gross revenues it earned for the month, and if the percentage rent exceeds the monthly MAG, it is to pay the excess by the 20th of the following month. Bay Area Group always paid more than the monthly MAG each month, and correctly paid its rent, including the portion of the MAG that should have been paid the previous month. Nevertheless, Bay Area Group underpaid its MAG by \$2,230 each month, and was at least one month late in paying the monthly MAG from March 2005 through December 31, 2006. According to Airport staff, it would be too difficult to determine the cause of the MAG billing error since it happened several years ago; however, the Airport has recently implemented a new billing system which it believes will prevent such problems in the future.

**Bay Area Group's  
Deposit for Buena Vista  
Café is Insufficient**

As of 2007, Bay Area Group's security deposit for Buena Vista Café was \$13,103 less than required by its lease agreement. The agreement states that the security deposit, which is in the form of a bond payable to the City, must be equal to one-half of the current MAG. Because the MAG also increased for 2008, Bay Area Group should ensure that it increases its deposit to an amount that is one-half of the current MAG.

**The Airport's Accounts  
Receivable Balances  
Should be Reviewed and  
Adjusted**

Our review of the Airport's outstanding accounts receivable for our audit period disclosed that Bay Area Group had 11 credits and 8 outstanding invoices, totaling a net of \$524 owed. The credits ranged from \$18 to \$3,709, while the amounts owed by Bay Area Group ranged from \$23 to \$4,070. We also found an erroneous credit of \$400 that should actually be recorded as \$400 owed. These transactions did not include one outstanding credit of \$79,012 for construction improvements by Bay Area Group. Bay Area Group's controller was not aware of any payments owed or of the large credit.

In confirming these amounts, we discovered that the Airport did not always apply payments to the proper accounts in accordance with Bay Area Group's rent statements. This resulted in some of the credits and outstanding invoices we identified. Another contributing problem was a time lag involved between the issuance of the billing instruction for the annual MAG change and the implementation of the new MAG in January of each year. There was usually a lag of about three to four months. As a result, the Airport retroactively collected the increased MAG amount. However, the Airport generated bills for the increased MAG, which Bay Area Group had already paid through the percentage rent, but the Airport did not credit Bay Area Group for paying the increased MAG amount and retained the increases as part of its accounts receivable.

## **Recommendations**

The Airport should take the following actions:

1. Ensure that its new billing system has controls to prevent incorrect billing of the monthly MAG.
2. Follow up with Bay Area Group to ensure it increases its security deposit for Buena Vista Café to one-half of the current MAG.
3. Review and correct its outstanding accounts receivable records for Bay Area Group, and clear the amounts due or credited that are, in fact, already paid or cleared.
4. Formally advise Bay Area Group of the large outstanding credit of \$79,012 and determine how the credit should be applied.

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# ATTACHMENT: AIRPORT'S RESPONSE

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San Francisco International Airport

February 10, 2009

P.O. Box 8097  
San Francisco, CA 94128  
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www.flysfo.com

Mr. Robert Tarsia  
Deputy Audit Director  
Office of the Controller  
City and County of San Francisco  
City Hall  
1 Dr. Carlton B. Goodlett Plaza  
San Francisco, CA 94102

AIRPORT  
COMMISSION  
CITY AND COUNTY  
OF SAN FRANCISCO

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LINDA S. CRAYTON  
VICE PRESIDENT

CARYL ITO

ELEANOR JOHNS

RICHARD J. GUGGENHIME

JOHN L. MARTIN  
AIRPORT DIRECTOR

Re: Audit of Domestic Terminals Food and Beverage Lease Nos. 03-0184,  
03-0202, and 03-0204 with Bay Area Restaurant Group – Airport's Response

Dear Mr. Tarsia:

The Airport's response is in the attached Audit Recommendation and Response Form, addressing each recommendation in the audit report.

We thank you for your staff's work on this audit. Please do not hesitate to call if you have any questions.

Sincerely,

A handwritten signature in dark ink, appearing to read "Cheryl Nashir", is written over a horizontal line.

Cheryl Nashir  
Associate Deputy Airport Director  
Revenue Development and Management

cc: Edwin De Jesus  
Leo Fermin  
Cesar Sanchez  
Gigi Ricasa  
Matthew McCormick



Recommendation	Responsible Agency	Response
The Airport should take the following actions:		
1. Ensure that its new billing system has controls to prevent incorrect billing of the monthly MAG.	Airport	The Airport's recently implemented a property management billing system (PMBS/ABM) which provides for automated adjustment of the MAG.
2. Follow up with Bay Area Group to ensure it increases its security deposit for Buena Vista Café to one-half of the current MAG.	Airport	Revenue Development & Management agrees with this statement, and will follow up with the tenant to ensure that their deposit is increased.
3. Review and correct its outstanding accounts receivable for Bay Area Group, and clear the amounts due or credited that are, in fact, already paid or cleared.	Airport	We will review the account of Bay Area Restaurant Group and adjust/correct the account as necessary.
4. Formally advise Bay Area Group of the large outstanding credit of \$79,012 and determine how the credit should be applied.	Airport	Credit memo has been applied against the following invoices: IR0809319101 (\$47,191.79) and IR0809319401 (\$31,820.41).

# ATTACHMENT: BAY AREA GROUP'S RESPONSE

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February 4, 2009



Robert Tarsia  
Deputy Audit Director  
Controller's Office  
City Hall, Room 316  
1 Dr. Carlton B. Goodlett Pl.  
San Francisco, CA 94102

Dear Mr. Tarsia,

We are responding to your letter dated January 6, 2009, to address the findings of the audit of Bay Area Restaurant Group Joint Venture (Bay Area Group) for the period February 15, 2005, through December 31, 2007.

- Finding 1: The Airport Did Not Collect the Correct MAG for Noah's Bagels and Max's Eat.

No action required by HMSHost as this finding has been addressed to the San Francisco Airport Commission.

- Finding 2: Bay Area Group's Deposit for Buena Vista Café is Insufficient.

HMSHost agrees with the finding above and has communicated this to the appropriate department in order to ensure that the security deposit is updated appropriately.

- Finding 3: The Airport's Accounts Receivable Balances Should be Reviewed and Adjusted.

No action required by HMSHost as this finding has been addressed to the San Francisco Airport Commission.

- Finding 4: Outstanding credit of \$79,012 for construction improvements by Bay Area Group.

HMSHost has already applied the credit to October 2008 prepayments and September 2008 percentage rent. Please refer to the check number 03174219 dated 10/17/2008.

Please feel free to contact me at (240) 694-4265 if you have any questions or need additional information.

Sincerely,

A handwritten signature in dark ink, appearing to read "Eswaran Jeyarajah".

Eswaran Jeyarajah  
Assistant Manager  
Contractual Compliance - Internal Audit





